

June 1996

CONTINGENCY OPERATIONS

Update on DOD's Fiscal Year 1995 Cost and Funding



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The Honorable Strom Thurmond
Chairman, Committee on Armed Services
United States Senate

The Honorable Floyd D. Spence
Chairman, Committee on National Security
House of Representatives

Contingency Operations:
updated on DoD's
Fiscal Year 1995 Cost
and Funding

The Department of Defense (DOD) participated in contingency operations in several places, including Haiti, Southwest Asia, and the former Yugoslavia during fiscal year 1995. To help cover the incremental costs¹ of these operations, the Congress provided DOD with a supplemental appropriation. We previously reported to you that while DOD ended fiscal year 1995 with supplemental funding of \$12 million above its reported incremental costs, some of the services and defensewide agencies as a whole had reported costs in excess of their supplemental appropriations while other services reported costs below their supplemental appropriations.² We also reported that costs surged in September 1995. Based on continued interest in these issues, we agreed with your offices to provide information on (1) how the services that reported costs in excess of supplemental funding covered their shortfalls and (2) why the surge occurred. We recently briefed your staff on these issues.

Background

The Congress appropriated \$253 billion for DOD for fiscal year 1995, of which \$92 billion was for operation and maintenance (O&M). Through fiscal year 1996, DOD's annual appropriations have not included funds for possible contingency operations. DOD has not budgeted for the incremental costs of military operations or contingencies. It has budgeted to be ready to conduct such operations. When the services have had to conduct these operations, the planned budget execution cycle was disrupted. DOD then had to absorb the incremental costs of these operations, which were mostly O&M items, within its appropriations or seek supplemental appropriations.

¹As used in this report, "incremental costs" means those costs that would not have been incurred if it were not for the operation. This is the same definition that is contained in 10 U.S.C. 127a, as amended by the fiscal year 1996 Department of Defense Authorization Act.

²Contingency Operations: Defense Cost and Funding Issues (GAO/NSIAD-96-121BR, Mar. 15, 1996).

In the Emergency Supplemental Appropriations and Rescissions for the Department of Defense to Preserve and Enhance Military Readiness Act of 1995 (P.L. 104-6), the Congress, in April 1995, provided DOD \$2,235 million for incremental costs associated with ongoing operations in a variety of locations, including Somalia, Rwanda, the former Yugoslavia, Haiti, Cuba, Southwest Asia, and Korea. The vast majority—91 percent—of the appropriation was for O&M. DOD reported fiscal year 1995 contingency operations-related incremental costs of \$2,223 million, \$12 million less than its supplemental funding.

In our March 1996 report, we stated that some of the services received fiscal year 1995 supplemental funding in excess of their reported costs. This excess funding was used for a variety of otherwise unfunded operational needs. Other services and defensewide agencies as a whole, on the other hand, reported costs that exceeded their supplemental appropriations.

Through August 1995, DOD had reported costs of \$1.9 billion. Projecting August costs to September, we estimated that had September costs been the same as August costs, DOD's full fiscal year 1995 reported costs would have been \$266 million below appropriated funding. However, reported September costs were about 4 times more than the costs of the previous month and over \$120 million more than the sum of the prior 3 months—June through August.

Results in Brief

The Army and the Navy reported incremental costs in excess of their O&M supplemental appropriations. While they covered their shortfall differently, both Army and Navy officials believe that unit readiness was not affected significantly. The reported shortfalls, however, may not be as great as reported costs suggest. We previously reported that some Army and Navy O&M costs were overstated. For example, in fiscal year 1995, we identified instances totaling \$33 million where the Army did not reduce its reported incremental costs for such things as normal operating costs not incurred and training not conducted due to participation in contingency operations.

The surge in September costs primarily related to (1) accounting adjustments; (2) end-of-fiscal year payments; and (3) other spending, including spending associated with higher operating tempo in Bosnia and Southwest Asia. We identified \$92 million in accounting adjustments and \$82 million in end-of-fiscal year payments, which together represented

60 percent of the September costs we examined. For example, we identified \$62 million in accounting adjustments made by the Army and the Air Force to reflect costs that should have been reported earlier in the fiscal year. Regarding year-end payments, the Air Force reported about \$47 million in payments for items such as communication requirements, support and base maintenance contracts, consumables, and landing fees. Over half of the \$47 million involved payments to other DOD components, such as the Army Corps of Engineers, and to contractors for expenses incurred in the last quarter of the fiscal year, although funds were not obligated until the end of the fiscal year to pay for them. The balance of these payments was for expenses incurred in September.

Scope and Methodology

To obtain information on how the Army and the Navy covered their differences between funding and reported costs, we reviewed service documents and met with officials in the military services, including those in selected major commands. We also discussed these matters with officials from the Office of the Secretary of Defense. Because we found in our March 1996 review that the vast majority of the differences between funding and reported costs was in O&M accounts, we focused our efforts on these accounts.

To obtain information on the surge in reported costs for September 1995, we reviewed the O&M appropriation accounts because they constituted the vast majority of that surge. We also analyzed DOD's monthly contingency operation incremental cost reports to identify the sources of the surge by service and operation, and we selected those operations that accounted for 88 percent of the reported September 1995 costs. We then reviewed service documentation supporting those operations and discussed the reasons for the surge with officials from the affected major commands and with service headquarters officials.

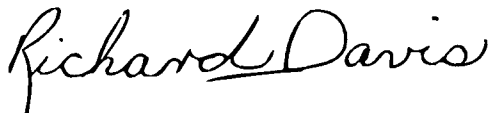
We previously reported that when considering the cost of operations, it should be recognized that DOD's financial systems cannot reliably determine costs. DOD's systems are classified as high risk, are not integrated, and cannot easily capture actual incremental costs. Only the total obligations are captured by the accounting systems. The services use various management information systems to identify incremental obligations and to estimate costs.

We performed our work between March and May 1996 in accordance with generally accepted government auditing standards. We reviewed the

information in this briefing report with DOD officials and made changes where appropriate. DOD officials generally agreed with our findings.

We are providing copies of this report to the Chairmen and Ranking Minority Members of the House and Senate Committees on Appropriations and to the Ranking Minority Members of the Senate Committee on Armed Services and the House Committee on National Security. We are also sending copies to the Secretaries of Defense, the Army, the Air Force, and the Navy and the Director, Office of Management and Budget. Copies will be made available to others upon request.

If you or your staff have any questions about this report, please contact me at (202) 512-3504. The major contributors to this report are listed in appendix I.

A handwritten signature in black ink that reads "Richard Davis". The signature is written in a cursive style with a large, stylized "R" and "D".

Richard Davis
Director, National Security
Analysis

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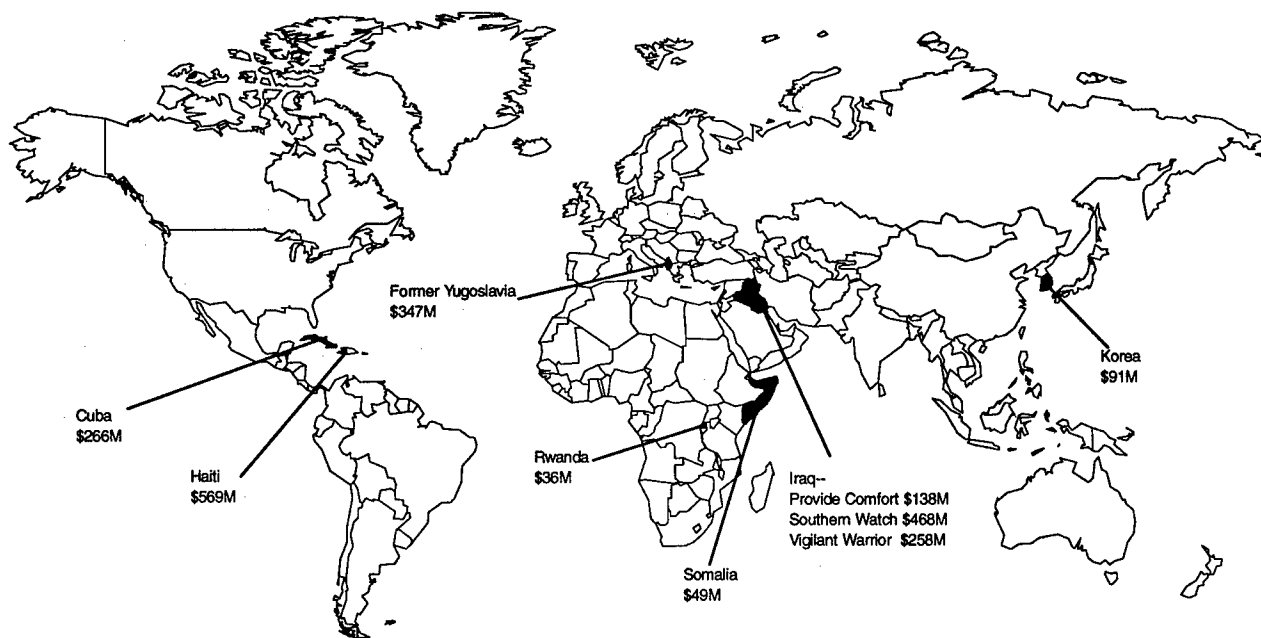
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Abbreviations

DOD	Department of Defense
O&M	operation and maintenance

Background

GAO Reported Incremental Costs for Fiscal Year 1995 Operations

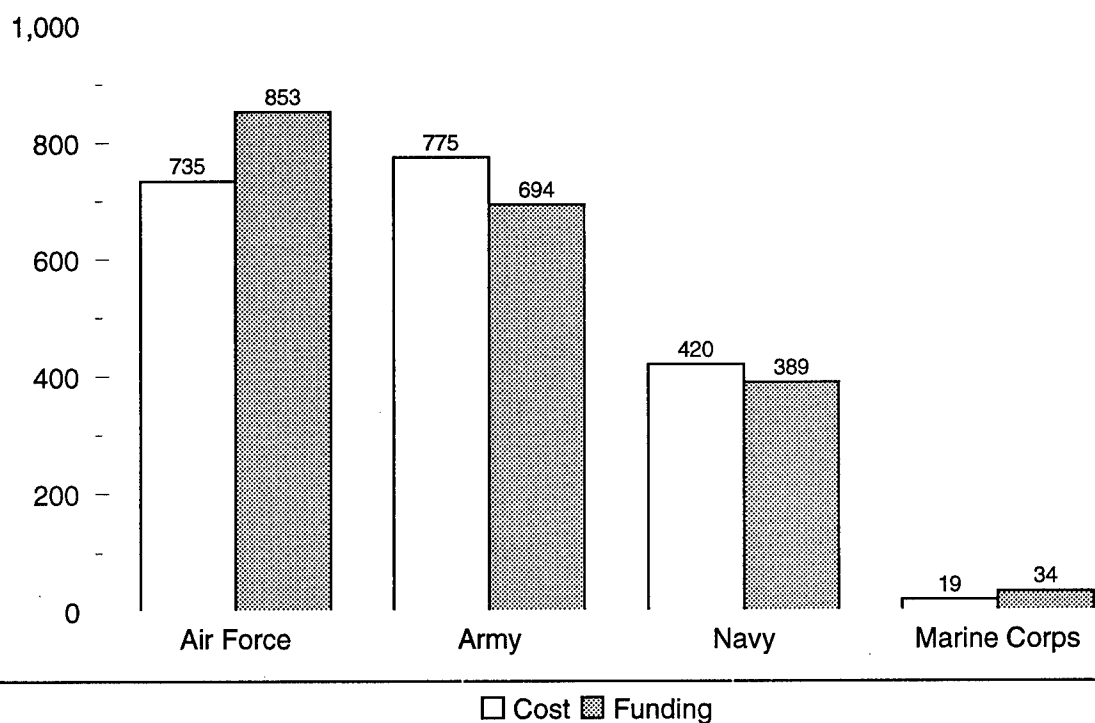


The Secretary of Defense's 1995 Annual Report to the President and the Congress describes contingency operations as military operations that go beyond the routine deployment or stationing of U.S. forces abroad but fall short of large-scale theater warfare. U.S. military forces participated in several contingency operations during fiscal year 1995. These operations included (1) activities in support of United Nations peace operations in Haiti, Southwest Asia, and the former Yugoslavia; (2) the increased deployment of military capability to South Korea in response to heightened tensions; (3) the deployment of additional military forces to Kuwait and Saudi Arabia in response to the threat of renewed Iraqi aggression against Kuwait; and (4) the enforcement of a revised U.S. policy designed to prevent Cuban migrants from reaching the United States. The map shows where these operations occurred and the Department of Defense's (DOD) reported incremental costs for each operation.

Most of DOD's reported incremental costs are for operations in four areas—Southwest Asia, Haiti, Cuba, and the former Yugoslavia. These costs total about \$2 billion, or 92 percent of DOD's total reported incremental costs. Within Southwest Asia, DOD participated in operations to (1) enforce United Nations sanctions against Iraq, (2) enforce the no-fly zone over both northern and southern Iraq, and (3) provide humanitarian relief to the population of northern Iraq.

GAO Services' Fiscal Year 1995 O&M Incremental Costs and Funding

Dollars in millions



In April 1995, the Congress provided DOD with an emergency supplemental appropriation of \$2,235 million to fund contingency operations occurring in fiscal year 1995. The vast majority—91 percent—of the appropriation was for operation and maintenance (O&M), which funds the operating costs of a deployment, such as transportation and contractor support. The balance of the appropriation was for military personnel accounts, which fund the cost of incremental pay, such as imminent danger pay. Through the end of fiscal year 1995, DOD reported about \$2,223 million for contingency operations-related incremental costs. Therefore, DOD ended the fiscal year with supplemental funding of \$12 million above its reported incremental costs. However, some of the services and defensewide agencies as a whole reported costs that were in excess of their supplemental appropriations, while other services reported costs below their supplemental appropriations.

The Army and the Navy reported O&M incremental costs of \$81 million and \$31 million, respectively, in excess of their supplemental funding. Defensewide agencies collectively reported O&M incremental costs of \$3 million in excess of their supplemental funding. The Air Force and the Marine Corps reported incremental O&M costs that were less than their supplemental O&M funding. The Air Force received \$118 million more in O&M supplemental funding than its reported costs; the Marine Corps \$15 million more. Both services used their excess O&M funding for a variety of otherwise unfunded operational needs.

How Services Absorbed Funding Shortfalls

GAO

Army's Reported O&M Costs Exceeded Supplemental Funding

	<u>Dollars in millions</u>
Reported O&M contingency costs	\$775
Supplemental O&M funding	<u>694</u>
Difference	81
How the Army covered difference	
Special reserve fund	\$41
Nonreadiness accounts	40

The Army reported \$81 million more in O&M incremental costs than its O&M supplemental appropriation. The Army absorbed this shortfall within its fiscal year 1995 appropriation. Army officials told us that \$41 million was funded through a special reserve fund, which is created at the beginning of each fiscal year for senior leadership to (1) take advantage of opportunities that arise throughout the year and/or (2) cover unbudgeted expenditures in the year of execution. In fiscal year 1995, this fund was created by requiring the commands to provide a total of \$50 million, less than one-half of 1 percent of the active Army's \$18 billion O&M appropriation.¹ The remaining \$40 million was absorbed within nonreadiness accounts, resulting in some unfunded nonreadiness requirements, such as environmental and construction requirements to initiate base closures. According to Army officials, unit readiness was not affected by the \$81-million shortfall.

The Army's reported shortfall may not be as great as its reported costs suggest. We previously reported that some Army O&M costs were overstated.² The Army has not offset its reported incremental costs to reflect costs that are not incurred when soldiers are deployed for contingency operations. For example, in fiscal year 1995, we identified instances totaling \$33 million where the Army did not reduce its reported incremental costs for such things as (1) normal operating costs not incurred and training not conducted due to participation in contingency operations and (2) items purchased but not used and either retained by the unit or returned to the DOD supply system for credit that was not deducted from reported incremental costs. We did not identify any instances of underreporting of O&M costs.

¹The remaining \$9 million of the special reserve fund was spent on such activities as funding the Commission on Roles and Missions of the Armed Forces and reviewing information systems and consolidations in the Army.

²Contingency Operations: DOD's Reported Costs Contain Significant Inaccuracies (GAO/NSIAD-96-115, May 17, 1996).

GAO Navy's Reported O&M Costs Exceeded Supplemental Funding

	<u>Dollars in millions</u>
Reported O&M contingency costs	\$420
Supplemental O&M funding	<u>389</u>
Difference	31
How the Navy covered difference	
Emergency supplemental for flying hours	\$11
Command absorption	20

The Navy reported \$31 million more in O&M incremental costs than its supplemental appropriation. The Navy's Pacific Fleet had the bulk of the shortfall, almost two-thirds, or \$20 million. To help cover the shortfall, Navy headquarters provided the Pacific Fleet with \$11 million in additional funds. These funds were drawn from \$41 million the Navy was allotted for flying hours in emergency supplemental funds beyond those funds the Congress provided for the cost of contingency operations. The Pacific Fleet absorbed the balance of its shortfall—\$9 million—by deferring funding for base support programs.

The Navy Comptroller office provided us documentation indicating that the other Navy commands with significant shortfalls either deferred or reduced spending to absorb their shortfalls. The Naval Reserve Force covered its \$4.4-million shortfall by deferring funding for helicopter and aircraft maintenance. The Naval Air Systems Command covered its \$3-million shortfall by deferring or reducing funding for tactical systems software programs, transportation requirements, and other programs. The Navy Computers and Telecommunications Command funded its \$2-million shortfall by deferring funding for the maintenance of real property at facilities in both the Atlantic and Pacific regions. The Chief of Naval Personnel covered its \$1.1-million shortfall by reducing purchases of subsistence items. According to the Navy Comptroller office, the deferrals and reductions in program funding were made in programs where the least negative readiness impact would occur.

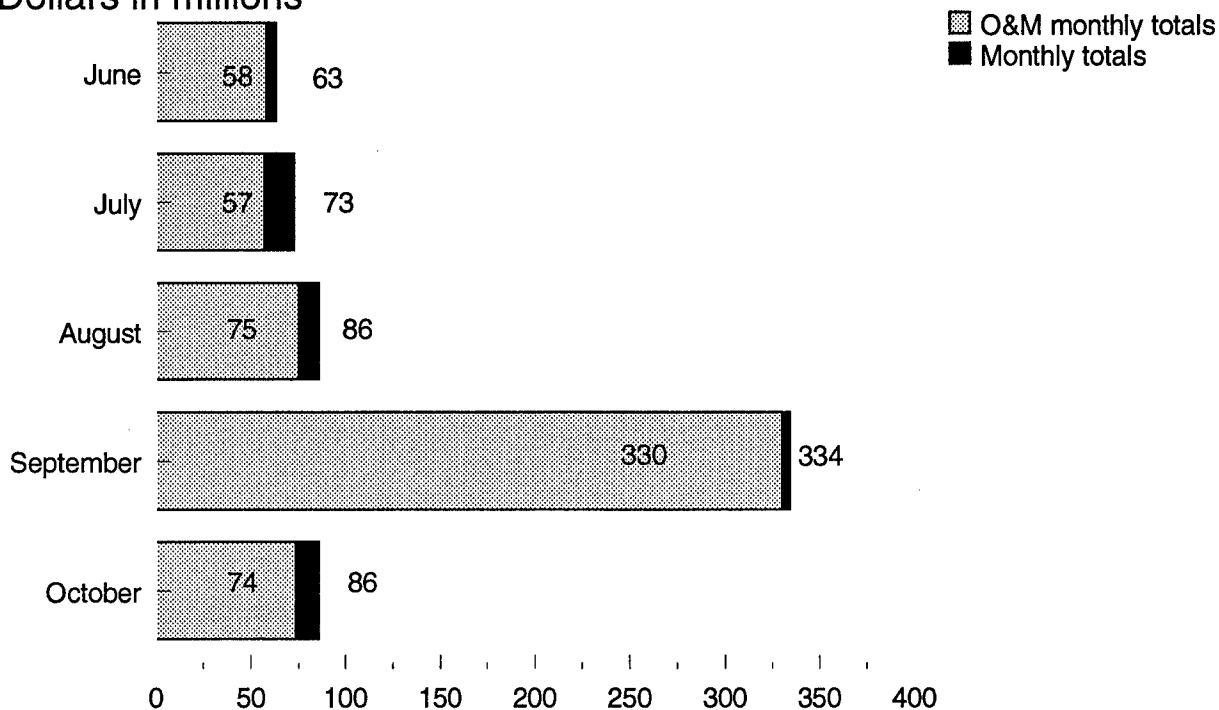
As was the case with the Army, we recently reported that the shortfall may not be as great as the reported costs suggest. We found an instance where the Navy may have overstated its costs in fiscal year 1995 because it did not adjust incremental flying hour costs to reflect over \$1 million worth of free fuel received.³ While the Navy has advised us that it does account for free fuel in its flying hour cost factors, it did not provide any documents to support this position. While we identified instances of underreporting Navy procurement costs in fiscal year 1995 in our report on the accuracy of contingency cost reporting, we did not identify any instances of underreporting of O&M costs.

³In some cases, the United States is provided fuel by other nations at no cost for U.S. ground, air, and naval forces during contingency operations.

Reasons for September O&M Cost Surge

GAO Reported Incremental Costs Surged in Late Fiscal Year 1995

Dollars in millions



We previously reported that through August 1995, DOD had reported costs of \$1.9 billion. Projecting August costs to September, we estimated that had September costs approximated August costs, DOD's full fiscal year 1995 reported costs would have been \$266 million below appropriated funding. However, reported costs surged in September to bring reported costs within \$12 million of the funding provided through the supplemental appropriation. The reported September costs were about 4 times more than the costs of the previous month and over \$120 million more than the sum of the prior 3 months—June through August.

The surge in costs was due to a sharp increase in reported September 1995 O&M costs. Between August and September 1995, reported O&M costs increased from \$75 million to \$330 million. O&M costs then declined to \$74 million in October 1995, the first month of fiscal year 1996, suggesting that September costs were atypical.

Except for the Marine Corps, each of the military services and other DOD agencies, such as the Defense Health Program and the Defense Mapping Agency, reported a collective increase of \$256 million in September over August O&M costs. The Army and the Air Force reported the largest increases, \$112 million and \$106 million, respectively. The Navy reported a smaller increase, \$35 million, and other DOD agencies collectively reported the smallest increase, \$3 million. The Marine Corps reported September costs that were about \$1 million below August costs.

GAO Principal Reasons Why Reported O&M
Costs Surged in September

Dollars in millions

Accounting adjustments	\$92
Year-end payments	82
Other	118

The surge in September O&M costs primarily related to (1) accounting adjustments and (2) end-of-fiscal year payments. As previously noted, we examined 88 percent of reported September costs, or \$292 million of the \$330 million. We identified \$92 million in accounting adjustments and \$82 million in end-of-fiscal year payments, which together represented 60 percent of the amount we examined and more than half of all reported September costs.

The balance of the O&M costs reviewed was \$118 million. Some of these costs related to higher operating tempo costs, including flying and steaming hours for operations involving the former Yugoslavia and Iraq. In the case of the former Yugoslavia, the pace of operations increased during the bombing campaign in Bosnia that began in late August and ended September 22, 1995. In September 1995, the Air Force and the Navy reported O&M costs of \$49 million and \$17 million, respectively, involving the former Yugoslavia, an increase of \$25 million and \$10 million, respectively, above reported August 1995 costs.

In the case of Iraq, operations increased as the United States provided support for Jordan while that country provided asylum for two high-level Iraqi defectors. These costs related to Operation Southern Watch. The Navy reported \$29 million in Southern Watch O&M costs in September 1995, or more than 3 times reported August O&M costs of \$8 million. Of the September 1995 reported costs, the Navy's Pacific Fleet reported costs of about \$25 million, including \$17 million for air and ship operations attributed to both the aircraft carriers USS Lincoln and USS Independence being deployed in the Persian Gulf area, and an additional carrier, USS Nimitz, preparing for deployment. During September 1995, the USS Lincoln and the USS Independence conducted 24-hour, "around the clock," operations in which one carrier supported 12 hours of operations as normal when operating alone in the Gulf, and the other carrier conducted operations for the other 12 hours. This effectively doubled the Pacific Fleet's costs for air and ship operations for the month of September in that region.

GAO Accounting Adjustments ^a

	<u>Dollars in millions</u>
Omissions	\$62
Reimbursements	<u>31</u>
Total	93

^aTotal in this chart does not match the accompanying text and the preceding chart due to rounding.

The services, in finalizing their financial data at the end of the fiscal year, made accounting adjustments for a variety of reasons. These reasons included correcting errors and omissions. Both the Army and the Air Force adjusted their reported costs to reflect omissions. For example, the Air Force included in its September report \$24 million in Korea costs that we were told should have been reported throughout the year. This amount reflected the cost of operating and maintaining more aircraft than

anticipated because of heightened tensions on the Korean peninsula. According to an Air Force official, while costs for these aircraft were being incurred throughout the fiscal year, through an administrative oversight prior to September 1995, the Air Force had not been including them in its contingency cost reporting. Upon recognizing this and the need to properly report these costs as contingency related, Air Force officials told us that they took action to do so in late fiscal year 1995 and included all these costs incurred throughout the fiscal year in the September 1995 cost report.

The Air Force also adjusted reported costs to include (1) about \$17 million in costs associated with aircraft maintenance in Southern Watch that were incurred before September but were not reported earlier due to an administrative error and (2) \$1 million in costs associated with operations in the former Yugoslavia that had not been included in its contingency cost reporting. The Army erroneously deleted \$20 million in cumulative Haiti costs from its August cost report, which it corrected by including the cost in its September report.

The Army also adjusted its cost reporting to include (1) \$25 million in Operation Southern Watch costs to correct overbilling of Kuwait and (2) \$6 million in reimbursement it received from the Department of State. In the case of Kuwait, the government of Kuwait reimburses the Army for some costs associated with exercises conducted in that country. Exercises are not considered contingencies and so are normally not included in contingency cost reporting. The Army does not include the reimbursed exercise costs in its contingency cost reporting. However, the Army billed Kuwait, and Kuwait paid \$25 million for exercise costs that were really contingency costs. Subsequently, the Army reimbursed Kuwait and revised its September contingency cost report to reflect this adjustment.

The Army does not include costs incurred on behalf of other U.S. government agencies in its contingency cost reporting if it is reimbursed by those agencies. Until it is reimbursed, the Army pays and reports these costs. The Army had been incurring and reporting costs involving the Department of State. When it was reimbursed by the Department of State, it reduced its August costs by \$6 million to reflect the reimbursement. The reduction had the effect of making the change between August and September costs appear to be \$6 million higher than it actually was.

GAO Year-end Payments

	<u>Dollars in millions</u>
Air Force	\$65
Army	8
Navy	<u>9</u>
Total	82

Part of the surge in reported costs related to end-of-fiscal year payments. Among the services, the Air Force had the largest amount of such payments, totaling \$65 million. Of this amount, the Air Force reported about \$47 million for items such as communication requirements, support and base maintenance contracts, consumables, and landing fees. Over half of the \$47 million involved payments to other DOD components, such as the Army Corps of Engineers, and to contractors for expenses incurred in the last quarter of the fiscal year, although funds were not obligated until the end of the fiscal year to pay for them. Consequently, these costs were reported in the September cost report when the funds were obligated. The balance of these payments was for expenses incurred in September. The remaining Air Force year-end payments related to \$18 million in estimated transportation costs for September in anticipation of billings. The Army also reported \$8 million in payments to pay transportation bills both received earlier in the fiscal year and in anticipation of further billings. The Navy reported almost \$9 million in payments for a September airfield rental billing and to support Navy P-3 operations in Oman.

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